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No. 83-978

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

SAMUEL MOORE AND COMPANY and
EATON CORPORATION,
Petitioners,

vs.

MULTIFLEX, INC.,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

REPLY BRIEF FOR THE PETITIONERS

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REPLY BRIEF FOR THE PETITIONERS

As this case shows, there is much confusion in the law of attempt to monopolize. The lower courts, like the court below, have often failed to recognize that monopoly power cannot be maintained in the absence of significant barriers to entry. This case is a clear example of the results of this confusion in the lower courts. Multiflex's rapid success in the market and the concomitant rapid erosion of Moore's market position here clearly show (1) Moore's lack of market power, (2) the absence of barriers to entry and, thus, (3) the absence of any possibility, much less a dangerous probability, of monopolization.[1]

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[1] The long-standing conflict and confusion concerning the attempt to monopolize offense is not restricted to the Ninth Circuit. The decision below

(footnote continues)

Multiflex would have this Court focus only on the market position that Moore enjoyed before it was challenged by Multiflex and the alleged difficulty that Multiflex faced in taking away over half of Moore's market within only two years and with an initial investment of only $550,000. The statement of the claims is alone enough to highlight its weakness. Moore's obvious inability to exclude Multiflex from the market, or even to keep Multiflex from achieving a dominant share of the market, shows clearly enough the absence of any possibility of monopoly power. The absence of competitors is not necessarily monopoly power, any more than the absence of temptation is virtue. The fact that the courts below could nonetheless find a "dangerous probability of success" here highlights the need for this Court to clarify what constitutes a "dangerous probability" of success in a section 2 attempt case.

I.

An Analysis Of The Competitive Structure Of The Market Is An Essential Predicate To Any Finding Of An Attempt To Monopolize.

Contrary to what Multiflex suggests, Moore does not argue that "success" in obtaining or maintaining a monopoly is a prerequisite to proof of a section 2 attempt claim. (Brief in Opp. at 9). Moore argues that some analysis of the likelihood of monopoly—the "dangerous probability of success"—is necessary to make out a section 2 claim. The court below did not undertake the proper analysis.

The lower court's "analysis" was critically deficient because it failed to examine the competitive facts of the relevant market, focused solely on Moore's beginning market share, and ignored completely what happened in the marketplace. Multiflex's assertions aside, Moore does not focus "solely on the

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(footnote continued)

provides an excellent example of the general confusion and conflict which can only be remedied by this Court. Multiflex disputes neither the existence of this conflict nor the need to resolve it.

market share after" Multiflex's entry into the market; it focuses on the competitive facts which resulted in that decreased share.[2]

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[2] Moore pointed to a number of cases in its petition, including *Nifty Foods Co. v. Great Atlantic & Pacific Tea Corp.*, 614 F.2d 832 (2d Cir. 1980), because these cases reflect a proper appreciation for the significance of a defendant's declining market share and demonstrate a conflict in approach with the decision below. The cases cited by Multiflex in its brief in opposition are not contrary:

In *Broadway Delivery Corp. v. United Parcel Service of America, Inc.*, 651 F.2d 122 (2d Cir. 1981), *cert. denied*, 454 U.S. 968, the court affirmed a jury finding for the defendant on a monopolization claim and held that it was harmless error to instruct the jury that to have monopoly power the defendant must have possessed at least 50 percent of the market. The court explained that in *Nifty Foods*, it did not affirm the defendant's judgment "simply because 48.3% was less than 50%." 651 F.2d at 128. Rather, there the court *assessed the significance of the defendant's share, "specifically noting that the share had steadily declined to 33%."* 651 F.2d at 128 (emphasis added). The court cited with approval *Berkey Photo Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 273 n.11 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093, which also recognized the significance of a decline in the defendant's market share. 651 F.2d at 128.

Greyhound Computer Corp. v. International Business Machine Corp., 559 F.2d 488 (9th Cir. 1977), *cert. denied*, 434 U.S. 1040, was premised on the Ninth Circuit's unique rule that dangerous probability of success is not an independent element of attempt to monopolize, and supports Moore's position that there is great confusion in the lower courts as to the scope of the attempt offense and what proof of a "dangerous probability" of success requires.

American Tobacco Co. v. United States, 328 U.S. 781, supports the position that a "dangerous probability of success" is a separate element of a section 2 attempt claim insofar as it cites with approval the lower court's jury instructions to that effect.

In *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255 (7th Cir. 1981), *cert. denied*, 455 U.S. 921, the district court rejected the plaintiff's contention that the defendant possessed sufficient market power to create a dangerous probability of monopoly because the defendant's profits and market share had steadily declined after the alleged attempt. The appellants argued that this declining performance was totally irrelevant because it occurred after the alleged attempt to monopolize. The court of appeals rejected the appellant's argument, stating that they had failed to cite any authority "which would require exclusion of the evidence of the later period of time" and citing *Nifty Foods* for the contrary position. 660 F.2d at 270. The court held that while not necessarily dispositive, *the defendant's market performance subsequent to the alleged attempt was relevant to whether the defendant ever had the actual ability to achieve a monopoly*. 660 F.2d at 271.

To establish the likelihood (or "dangerous probability") of monopoly, Multiflex and the court below relied solely on the fact that, before Multiflex ever began to compete with Moore, Moore had a significant market share.[3] But beginning market share by itself proves nothing, other than who made what share of sales in a given period. This Court has recognized that exclusive focus on market share can produce a distorted image of market power because "the relative effect of percentage command of a market varies with the setting in which the factor is placed." *United States v. Columbia Steel Co.*, 334 U.S. 495, 528. A true picture emerges only from a careful analysis of the competitive structure of the market. Thus, "[i]f the industry is one in which . . . outsiders could rapidly enter if prices were pushed significantly above competitive levels, even a share as large as 90% . . . may not confer massive" market power. L. Sullivan, *Antitrust* § 23 (1977). On the other hand, the fact that there were no demonstrated barriers to entry and that Multiflex not only succeeded in entering the market but came to dominate the market are compelling indicators of Moore's lack of market power.

The courts below did not attempt a competitive analysis, but instead merely inferred the existence of market power from Moore's market share before Multiflex entered the market. This is bad law and bad policy. The Court should make clear that such inferences, contrary to fact, are not sufficient to support conclusions such as those drawn by the court below.[4]

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[3] The Court below never made a finding that Moore possessed monopoly power in the market for hydraulic hose bundles. The evidence does not indicate that Moore was either able to raise prices and restrict output or to exclude competitors from the market—the traditional earmarks of monopoly power. Instead, in its brief in opposition, Multiflex attempts to prove the existence of such power by repeatedly claiming that Moore "forced" the three OEMs into conspiring not to deal with Multiflex. Allegedly, the OEMs agreed with Moore to exclude Multiflex because they thought Moore otherwise might succeed in excluding Multiflex from the market. This unlikely scenario cannot substitute for a showing of real economic market power, even if it were true, which it clearly is not.

[4] The Assistant Attorney General of the Antitrust Division of the United States Department of Justice recently stated that the Division will only direct

(footnote continues)

II.

Respondent's Analysis Of The Existence Of Entry Barriers In This Case Highlights The Need For This Court To Clarify What Constitutes An Antitrust "Barrier To Entry."

The concept of barriers to entry is at the economic core of section 2; an attempt to monopolize cannot present a "dangerous probability of success" if the offender is in fact not able to exclude new entrants.[5] Yet, as the respondent's brief in opposition and the decision below demonstrate, the concept of barriers to entry is easily misused to support results which are inconsistent with the purpose of the antitrust laws. Unless this Court clarifies what properly constitutes a "barrier to entry" in the antitrust sense, "it will remain impossible to make antitrust laws more rational or . . . to restrain the growth of its more powerful irrational elements." R. Bork, *The Antitrust Paradox* 310 (1978). This case—in which a new entrant became the dominant firm by the end of its second full year in business—is the perfect case in which to address this point.

The proper issue is whether there exist *artificial* barriers to entry which prevent new firms from effectively challenging a

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(footnote continued)

its enforcement efforts at "truly anticompetitive conduct that unreasonably threatens to eliminate competition in particular markets" and will carefully analyze the economic effects on the market of single-firm conduct before bringing enforcement actions. Statement of J. Paul McGrath, Before the Subcmte. on Monopolies and Commercial Law, House Cmte. on the Judiciary Concerning Antitrust Division's Authorization for Fiscal Year 1985, February 2, 1984.

[5] A barrier to entry in the antitrust sense is a condition that makes the costs of a new entrant higher than the costs of a firm already in the market:

> The existence of such a condition creates a range within which the firms in the market can raise the market price above the competitive level without attracting new entry. If the marginal cost of a firm in the market is $4 and the marginal cost of a new entrant is $5, the firms in the market can charge up to $5—a supracompetitive price—without fear of inducing entry by a firm desiring to share in the supracompetitive profits generated by the monopoly price.

R. Posner, *Antitrust* 496 (1974).

"monopolistic" market position. If, as was the case here, new firms of superior or equal efficiency are able to enter the market, no antitrust concern is raised because the alleged "monopolist" is subject to the discipline of competition. The important question is whether new entry that would otherwise be drawn by supracompetitive profits is deterred because the new entrant faces artificially high marginal costs that would wipe out any profit at a competitive price. Thus, the market shares of firms already in the market have absolutely nothing to do with the existence or significance of barriers to entry. L. Sullivan, *Antitrust* 77-78 (1977).

Both Multiflex and the court below ignored the functional significance of barriers to entry. After the fact, Multiflex hypothesizes three barriers to entry in its brief in opposition: (1) Moore's patent relating to a particular type of hose used in hose bundles;[6] (2) the "capital structure required to enter the market"; and (3) the "established channel of marketing created by the close relationship between Moore and the OEMs." (Brief in Opp. at pp. 14-18). None of these "barriers" received scrutiny by the court below, nor can they bear any now. None constitute actual barriers to entry in the antitrust sense.

Multiflex's contention that Moore's patent constituted a barrier to entry ignores the facts that it was neither difficult nor costly (in terms of time or money) to invent around the patent and that the particular technology was not essential to entry into the market. Multiflex did not invalidate the patent, nor did it obtain a license, yet it still became the dominant firm in the market within two years. Although Multiflex suggestively reminds the Court that Moore sought to protect its patent by bringing a patent infringement suit against Multiflex, Multiflex does not suggest that Moore's suit was brought in bad faith or that the patent is invalid. This Court has repeatedly held that it is not the purpose of the antitrust laws to chill the enforcement of valid patents. *See Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 135 ("A patentee has the exclusive right to manufacture, use, and sell his invention. . . . The heart of his

[6] Although Multiflex refers to "a number of patents," it is undisputed that only one valid patent related to the hoses is involved in this case.

legal monopoly is the right to involve the State's power to prevent others from utilizing his discovery without his consent"); *see also Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405 (1908); *Crown Die & Tool Co. v. Nye Tool & Machine Works*, 261 U.S. 24 (1923). In any event, Multiflex's success is the best gauge of the strength of this so-called "barrier."

Capital requirements are a barrier to entry only when the cost of capital to the new entrant is higher than the cost to the existing firm; the *amount* of capital required for entry affects only the *rate* of entry.[7] However, Multiflex does not claim that its cost of capital was any higher than the cost of capital to Moore. Multiflex does assert that Moore somehow artifically increased the amount of capital required beyond what it otherwise would have been, but these allegations are completely unsupported by the record. There is no evidence that Multiflex incurred increased costs by going directly to end-users (much less that such increased costs could ever be substantial enough to constitute a barrier to entry), or that Moore blocked financing from either Gates or McConkey.[8]

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[7] "A barrier to entry should be distinguished from a condition which affects the *rate* at which entry can occur." R. Posner, *Antitrust* 476 (1974) (emphasis added). The larger the amount of capital required to enter the market on an efficient scale, the longer it presumably might take for entry to occur. But capital requirements, no matter how great, only affect the *rate* of entry, and do *not* constitute antitrust barriers to entry *unless* the cost of capital is appreciably greater to a new entrant than to an existing firm. (The capital cost to an existing firm is a current cost, since the firm must reinvest capital continuously to replace worn or obsolescent productive assets.) *Id.*

[8] Multiflex also claims that the "amount of money to enter this particular market was high compared to the potential market itself." (Brief in Opp. at p. 18). First, as stated above, Multiflex introduced no evidence at trial to support a claim that the cost of selling directly to end-users was appreciably higher then selling to OEMs. Second, Multiflex's own success in the market by selling to end-users belies this argument. If the cost of selling directly to end-users was truly higher than the potential market justified, as a rational firm, Multiflex would not have entered the market, and, if it did, would not have succeeded. In any event, it is clear that the amount of capital required to enter the market was extremely small—roughly the equivalent of investment in a single gasoline station or McDonald's franchise in a large city. *See 1984 Franchise Annual Handbook and Directory* 68 (1984) (indicating that a $300,000 investment is necessary to obtain a McDonald's franchise).

Multiflex argues that "probably the most difficult barrier to entry" was the "established channel of marketing created by the close relationship between Moore and the OEMs." (Brief in Opp. at p. 15). However, the record in this case shows that this "established channel" was neither difficult nor a barrier to entry in the antitrust sense. Even a predatory disruption of distribution channels does not constitute a barrier to entry unless the distribution channel that is "closed off" is "so much more efficient then the alternative that those forced out of the pattern cannot compete." R. Bork, *The Antitrust Paradox* 158 (1978). In other words, the foreclosure of one pattern of distribution, to be a barrier to entry, must either impose significant costs on potential competitors that raise their marginal costs above a level which would allow them to earn any profit at a competitive price or make it impracticable to operate. Illustrative of this type of barrier to entry are the "essential facility" cases where a competitor is denied access to an essential economy of scale—such as, for example, where a board of trade expels or threatens to expel a member (*Board of Trade of Chicago v. United States*, 246 U.S. 231), or a stock exchange discontinues an essential connection between an independent broker and members of the exchange (*Silver v. New York Stock Exchange*, 373 U.S. 341).

Even if Multiflex were foreclosed from marketing through the OEMs,[9] the record contains no evidence that marketing directly to the end-users imposed any inefficiencies and costs on Multiflex, much less of a magnitude that Multiflex was unable to compete with Moore. Indeed, the evidence is dramatically to the contrary: by selling directly to the end-users, Multiflex came to dominate totally this market within two years.

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[9] There is no evidence in the record that Multiflex was actually foreclosed from marketing its product through the OEMs. The court of appeals found that Multiflex had failed to show that it suffered any injury due to the alleged conspiracy between Moore and the OEMs. (Pet. App. A at 12a-13a). Indeed, there was evidence in the record that at least one OEM purchased hose bundles from Multiflex during the period of the alleged conspiracy. (Pet. App. A at 5a; Cross-Pet. at 5).

The court of appeals did not discuss or consider the competitive structure of the market in question. If it had focused on competitive reality, especially the total absence of any significant barriers to entry, it would not have found any "dangerous probability" of monopoly. Decisions like the one below are the inevitable result of the confusion in the lower courts.

CONCLUSION

This Court should instruct the courts below to examine the competitive structure of the market in question and especially to consider whether there are any significant barriers to entry. When a market cannot be monopolized because there are no barriers to entry, there can be no dangerous probability of monopolization, and, as a matter of law, no attempt to monopolize violation can be found. That is what should have happened in this case, and this Court should so hold.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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